



## FEI Holds Conference on Current Financial Reporting Issues

Financial Executives International (FEI) recently held its 33<sup>rd</sup> annual conference on current financial reporting issues, including developments at the FASB, SEC, and PCAOB.<sup>1</sup> Panelists included representatives from standard setters, regulators, preparers, and accounting firms. This edition of *Defining Issues* discusses highlights from the conference.

### Key Facts

- The FASB is focused on improving its efficiency and effectiveness of operations and reducing complexity.
- Regulators and standard setters remain committed to providing timely interpretative guidance on the new revenue recognition standard. Successful implementation of the new standard was a common theme.
- Regulators and standard setters are focused on disclosure simplification and effectiveness.
- PCAOB representatives discussed recent inspection findings and are focused on improving audit quality.

Speakers from the FASB, SEC, and PCAOB stated that their views are their own and do not necessarily reflect the official views of their respective organizations.

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<sup>1</sup> Financial Executives International Current Financial Reporting Issues Conference, November 17-18, 2014, New York.

## FASB

Marc Siegel, FASB Board Member, and Cullen Walsh, FASB Assistant Director, discussed the FASB's cost-benefit analysis process, prioritization of projects, and agenda strategy. Mr. Walsh also discussed the purpose of the FASB/IASB joint Transition Resource Group (TRG) on Revenue Recognition and its future plans.

**Cost-Benefit Analysis.** Mr. Siegel said constituent feedback is essential to the FASB's cost-benefit analysis. The FASB's cost-benefit analysis considers both public and private companies as well as the time it would take and the need to modify or replace existing accounting systems to comply with new requirements.

**Transition Resource Group.** Mr. Walsh summarized the TRG's purpose, which is to address stakeholder concerns and inquiries that arise throughout the implementation phase of the new revenue recognition standard and to educate stakeholders on the new requirements to help them with implementation.<sup>2</sup> The TRG will not issue authoritative guidance. Instead, members of both the FASB and IASB (the Boards) will attend the TRG meetings and hear challenges directly from stakeholders. After hearing the feedback, the Boards may decide that stakeholders will benefit from more education or they may identify areas in which the new guidance can be improved. In limited cases (e.g., an aspect of the new guidance cannot be applied as intended), the Boards may add a narrow scope item to their agenda to complete or revise the new guidance in a consistent manner.

The TRG's meetings are open to the public and its staff papers are accessible online.<sup>3</sup> The TRG met twice in 2014 and four meetings are anticipated in 2015.<sup>4</sup>

Mr. Walsh also reminded stakeholders that they may submit their technical accounting inquiries to the FASB's Technical Inquiries Service.<sup>5</sup>

**Agenda Strategy.** Mr. Siegel discussed the FASB's efforts to address accounting complexities through foundational and simplification projects.<sup>6</sup> The foundational projects are meant to prevent *future* accounting complexities and include the conceptual, disclosure, and financial statement presentation framework projects.

Mr. Walsh discussed the FASB's simplification projects, which are meant to reduce cost and accounting complexities in *existing* U.S. GAAP while maintaining the usefulness of information.

<sup>2</sup> FASB Accounting Standards Update 2014-09, Revenue from Contracts with Customers, available at [www.fasb.org](http://www.fasb.org), and IFRS 15, Revenue from Contracts with Customers.

<sup>3</sup> Transition Resource Group papers are available at [www.fasb.org](http://www.fasb.org).

<sup>4</sup> See Defining Issues No. 14-49, Revenue Transition Resource Group Discusses Five New Issues, and Defining Issues No. 14-33, Revenue Transition Resource Group Holds First Meeting, both available at [www.kpmg-institutes.com/institutes/financial-reporting-network](http://www.kpmg-institutes.com/institutes/financial-reporting-network).

<sup>5</sup> Instructions on how to submit an inquiry to the FASB's Technical Inquiry Service are available at [www.fasb.org/inquiry/](http://www.fasb.org/inquiry/).

<sup>6</sup> See the FASB Technical Agenda at [www.fasb.org](http://www.fasb.org).

## SEC

James Schnurr, SEC Chief Accountant of the Office of the Chief Accountant, and Mark Kronforst, SEC Chief Accountant in its Division of Corporation Finance, updated attendees about the SEC's ongoing initiatives and potential future priorities.

Mr. Schnurr discussed three of the SEC's current focus areas:

1. **IFRS.** Mr. Schnurr and his staff are considering alternatives to IFRS in the United States. The project will require cost-benefit consideration and is not without significant legal and statutory hurdles. Mr. Schnurr's overriding message to constituents was to stay tuned.
2. **Audit Committee Disclosures.** The SEC staff is drafting a concept release on audit committee disclosures that would require an audit committee to disclose additional information in its proxy statement about the performance of its responsibilities, with a focus on the audit committee's oversight of the external auditor. This objective is to drive consistency and to further improve oversight of external auditors.
3. **Revenue Recognition.** Mr. Schnurr echoed earlier discussions on revenue recognition, observing that a number of implementation issues have not yet been addressed and that there is an overall need for additional guidance. Mr. Schnurr cited his obligation to U.S. investors including the successful implementation of the new standard and commitment to addressing the unanswered questions. Based on recent discussions with the FASB, Mr. Schnurr expects more timely activity.

Mr. Kronforst discussed additional areas of SEC focus, highlighting the need to provide information to investors in a more useful format (i.e., the EDGAR filing process is outdated) and to update outdated disclosure requirements.

Mr. Kronforst also discussed topics that the Division of Corporation Finance will focus on in future SEC filings:

- Foreign taxes;
- Chinese variable interest entities;
- Non-GAAP financial measures, particularly use of terms and metrics that are not defined in U.S. GAAP;
- Operating metrics; and
- Segments.

## PCAOB

Jay Hanson and Lewis Ferguson, PCAOB Board members, provided updates on the PCAOB and SEC's ongoing initiatives and potential priorities.

Mr. Hanson also discussed significant deficiencies in internal control over financial reporting that included the failure to:

- Identify and sufficiently test controls intended to address risks of material misstatement;
- Sufficiently test the design and operating effectiveness of management review controls;
- Obtain sufficient evidence to test the roll-forward period;
- Sufficiently test controls over system-generated reports;
- Perform sufficient procedures over the work of others; and
- Sufficiently identify and evaluate control deficiencies.

Mr. Ferguson discussed the PCAOB's audit quality initiative. Over 200 inspections of audit firms have been conducted. Many similar deficiencies seem to occur annually. The PCAOB is investigating root causes about why similar deficiencies continue to occur to help identify indicators of high quality audits.

The PCAOB expects to issue a concept release on audit quality.

## Audit Committee Roundtable

Current and former executives from major Fortune 500 companies discussed best practices and emerging issues faced by audit committees. While the panel agreed on many topics, different opinions were expressed about how detailed the disclosures should be in the annual report.

### Audit Committee Effectiveness

- **Culture.** The company's culture may be an indicator of risk.
- **Financial Controls.** An understanding of controls is needed to understand financial risk.
- **Effectiveness** of compliance programs.
- **Corruption.** Training employees to avoid corruption in the workplace.
- **Due Diligence.** Seek balanced viewpoints on the benefits and consequences of a transaction.
- **Diversity,** including diversity in skill sets.

### Primary Emerging Issues

- **Cybersecurity/Digital/Social Media,** including recruiting the right people with appropriate skill sets.
- **Activist Shareholders.**

## Controllers Roundtable

A panel of controllers from several leading companies discussed reporting and operational issues.

**Decentralization of Accounting Staff.** Panelists discussed the benefits of having accounting policy staff in the business units. This decentralized approach helps highlight potential accounting issues as business units negotiate contracts and transactions and gives accounting policy staff operational exposure.

**Close Process.** Panelists discussed strategies to accelerate the financial reporting close process and make it more efficient. Strategies discussed included using Six Sigma techniques to improve the close process and writing the annual report in the fourth quarter.

**COSO 2013.** Panelists adopting the 2013 Framework agreed that while it requires additional documentation, the 1992 Framework provides a good basis to meet the new framework's requirements.

## Emerging Trends in Year-end Reporting

A panel of representatives from major public accounting firms discussed issues that may impact year-end reporting and other financial reporting issues.<sup>7</sup> Topics discussed included:

- Implementation of COSO 2013;
- Continuation of efforts to implement the new revenue recognition standard;
- Consideration of new mortality tables and the potential impact on retirement plan obligations;<sup>8</sup> and
- The FASB's new standard on push-down accounting.<sup>9</sup>

## Revenue Recognition

Industry professionals from major companies and a representative from a major accounting firm discussed current implementation issues related to the new revenue recognition standard. A key theme in the discussions was the need to use judgment in applying the new standard.

<sup>7</sup> Public accounting firms represented on this panel included Deloitte, Ernst & Young, Grant Thornton, KPMG, and PricewaterhouseCoopers.

<sup>8</sup> For more information, see Defining Issues No. 14-48, Actuarial Issue New Mortality Data That May Affect Retirement Benefit Obligations, available at [www.kpmg-institutes.com/financial-reporting-network](http://www.kpmg-institutes.com/financial-reporting-network).

<sup>9</sup> FASB Accounting Standards Update No. 2014-17, Pushdown Accounting (a consensus of the FASB Emerging Issues Task Force), available at [www.fasb.org](http://www.fasb.org).

## Revenue Recognition Discussion Topics

### Identifying Performance Obligations

Panelists agreed that the guidance on the identification of performance obligations of a contract may include the following challenges:

- Determining whether delivery and installation are separate performance obligations; and
- Reviewing contracts in more detail to see if there are more performance obligations than under the previous standard.

### Revenue from License Agreements

Panelists noted that the new standard provides guidance on unique types of license agreements and that implementation efforts will need to consider more general license agreements. Some considerations include:

- Recording revenue for license agreements up-front or over time depends on the type of the license; and
- Developing a process to evaluate the large number of license agreements that many companies may enter into each year.

### Implementation

Panelists said that their companies have started the implementation process for the new standard, which may include the following initiatives:

- Dividing revenue streams into three groups: those that will be changed by the new standard, those that may be changed, and those that will not be changed;
- Reviewing samples of contracts and determining how they fit into the new model;
- Determining if there are any gaps in revenue recognition guidance from the current standard to the new standard; and
- Educating departments within the company including information technology, legal, and human resources.

In addition, some panelists have written position papers documenting the revenue process and how the process will fit into the new standard.

## Revenue Recognition Discussion Topics

### Transition

Companies are analyzing what they need to do to successfully transition to the new standard. Some panelist recommendations included:

- Know the transition method that other industry participants are leaning toward;
- Review the new disclosures required under the standard; and
- Keep open communication with auditors, management, and others within a company's industry.

Also, most had not determined which transition approach they would use, but they are in the process of gathering the necessary data to make that determination.

## Disclosure Simplification

Panelists from a cross section of companies and organizations discussed the need to make disclosures more effective. While standard setters are considering simplification initiatives, panelists discussed what preparers can do now including:

- Eliminate redundant disclosures and use cross references as appropriate;
- Eliminate immaterial as well as outdated information;
- Use plain English rather than jargon;
- Use tables and charts as appropriate instead of only using text; and
- Avoid adding disclosures just because the SEC may ask a question.

During another panel discussion, Mr. Kronforst from the SEC expressed general support for preparers to increase the effectiveness of their disclosures without being prompted by the SEC and the standard setters.

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